No. 93-1338

IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1993

J. ALEXANDER SECURITIES, INC.,

Petitioner,

vs.

SIGNE MENDEZ,

Respondent.

RESPONDENT'S BRIEF IN OPPOSITION

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QUESTION PRESENTED

WHETHER ARBITRATORS ARE PRECLUDED FROM AWARDING PUNITIVE DAMAGES WHEN THE PARTIES' SUBMISSION AGREEMENT, ALTHOUGH NOT SPECIFICALLY PROVIDING FOR PUNITIVE DAMAGES, INCORPORATES THE CLAIMANT'S DAMAGES CLAIM WHICH SPECIFICALLY SEEKS PUNITIVES, AND PETITIONER FAILS TO OBJECT TO THEIR CONSIDERATION.

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Federal Statutes

State Statutes

Rules

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Respondent Signe Mendez respectfully prays that Petitioner J. Alexander Securities, Inc.'s Petition for Writ of Certiorari be denied.

STATUTES AND REGULATIONS INVOLVED

1. Federal Statute

   9 U.S.C. §4

2. California Statutes

   Code of Civil Procedure

   §632
   §1286.6

3. NASD Code of Arbitration Procedure

STATEMENT OF THE CASE

The documents through which Respondent Signe Mendez originally opened her account with Petitioner J. Alexander Securities ("Petitioner") are not part of the record. However, submitted at the time of the arbitration as a document confirming Respondent did not have a discretionary account was one of the only documents bearing her signature, entitled "Cash Account Agreement," which provided that, in the event the client could not pay for

any particular trade, her account could be liquidated, i.e., "cashed out." (C8, pp. 164-165.) The document had nothing to do with the claims before the arbitration panel, which sought recovery for securities fraud, deceptive practices, account churning and inappropriate and unauthorized trades. The relevance of the "Cash Account Agreement" was established, as a matter of law at the Superior Court level [Beckett v. Kaynar Mfg. Co., Inc. (1958) 49 Cal.2d 695, 699] in a declaration by Petitioner's counsel, as confirming solely that Respondent did not sign a discretionary account form. (C8, pp. 164-165.) This document had nothing to do with the parties' choice of law at the arbitration, and may not be used now as a matter of law to establish choice of law.

Respondent amended her original claim solely at the request of Petitioner who sought more detail. The amended claim spelled out the specific dollar amounts sought and a request for attorneys' fees and punitive damages. (Court of Appeals Decision, Appendix, A5, fn. 4.) Petitioner's answer to the claim specifically acknowledged punitive damages were sought, and did nothing to contest the arbitrators' jurisdiction at this time over such damages. (Appendix, A5.) Rather, it merely argued throughout pursuant to California law that the facts did not support such damages. (Appendix, A5.)

The arbitration award granting punitive damages did so against the brokerage personally for its own "failure to meet its duty and obligation to adequately supervise [broker] Andrew E.

Webber, in that it did not come up to the standard of supervision required to assure compliance with applicable securities regulations." (Appendix, A6.) Punitive damages were not awarded based on vicarious liability or ratification of the broker's own acts and omissions.

The Petition to Correct filed before the Los Angeles County Superior Court sought to eviscerate the punitive damage award (while attempting to maintain both the compensatory damages which were substantially below what Respondent sought as well as the refusal to award attorneys' fees) by claiming the award of punitive damages violated Petitioner's right to due process. Petitioner also claimed that New York law applied, which barred an award of punitive damages. (Appendix, A6.) Because Petitioner sought to correct only part of the award, it was apparently

conceding that it received due process with respect to the compensatory damages and attorneys' fees, hence claiming that the three-person arbitration panel exercised two different due process standards. However, the Superior Court upheld the arbitration award; there was no statement of decision because Petitioner failed to request one timely. Code of Civ. Proc. §632.

Petitioner then appealed to the California Court of Appeals, Second Appellate District which, in a well-reasoned decision, affirmed the Superior Court decision. Pacific Mutual v. Haslip (1991) 499 U.S. 1, 111 S.Ct. 1032, 113 L.Ed.2d 1, was not given "short shrift" by the California appellate court; rather, it correctly held that Haslip did not control the analysis of the issues before it.

SUMMARY OF ARGUMENT

1. This case presents no issue appropriate for the Court's exercise of its discretionary jurisdiction. The underlying final and binding arbitration was tried pursuant to California law under which, in the absence of fraud, it is not reviewable as a matter of law or equity. California law further provides that punitive damages may be awarded when sought by the claimant if not expressly excluded. Such damages were specifically sought, fully litigated, and awarded under California law.

2. The court's opinion in Pacific Mutual v. Haslip does not raise due process considerations which are relevant to a binding securities arbitration. Nor does Haslip in any way deny arbitrators the authority to award punitive damages.

3. California law, not that of New York, was always the controlling law in this matter. Even, however, in the presence of New York law, California has already adopted the distinction between following the procedural versus substantive law of New York, which rule does not "ignore" the parties' choice of law and, further, is based on California's own pronounced public policy.

REASONS WHY THE WRIT SHOULD BE DENIED

I. THE ARBITRATION DECISION IS NOT, IN THE FIRST INSTANCE, REVIEWABLE AS A MATTER OF LAW OR EQUITY

The fatal flaw in Petitioner's entire argument is its attempt unilaterally to eviscerate a portion of a binding and final arbitration award after having full notice from the outset that the damages

sought by Respondent and considered by the arbitrators included punitive damages. Judicial review of this decision is limited to those specific and narrow statutory grounds set forth in Code of Civ. Proc. §1286.6, since "by voluntarily submitting to arbitration, the parties have agreed to bear [the risk of an erroneous decision by the arbitrator] in return for a quick, inexpensive and conclusive resolution to their dispute." Moncharsh v. Heily & Blase (1992) 3 Cal.4th 1, 11-12.

It is disingenuous at best to give any credence to the assertion that the only party which, in a securities arbitration, would be guilty of conduct warranting punitive damages must give its consent, in the true sense of "permission," to validate such an award. Indeed, carried to its logical conclusion,

such a holding could entitle the brokerage to "consent" only to damages below a certain dollar amount or to withhold "consent" to other basic rights held by a securities customer to be made whole, resulting in a brokerage-controlled sham proceeding which is anything but "alternative dispute resolution". Rather, "consent" in this context is logically determined by what has been submitted for consideration by either party to the arbitrators as defined by the scope of the dispute (i.e., here, the parties' relationship as brokerage/client). Such an interpretation is upheld by the California Supreme Court in Moncharsh, supra, 3 Cal.App.4th at 28: "It is within the 'powers' of the arbitrator to resolve the entire 'merits' of the 'controversy submitted' by the parties . . . (Section 1286.6 subd. (b)(c).) Obviously, the

'merits' include all the contested issues of law and fact submitted to the arbitrator for decision. The arbitrator's resolution of these issues is what the parties bargain for in the agreement." The record confirms through the appellate court's judicial notice of the underlying arbitration pleadings that the issue of punitive damages was clearly before them. The fact that punitive damages were "contested" as specifically envisioned by Moncharsh does not remove them from the scope of the issues before the arbitration panel[1].

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[1] Consistent by distinction with this analysis is the case cited by Petitioner of Thompson v. Jesperson (1990) 222 Cal.App.3d 964, in which attorneys' fees were voluntarily and unilaterally awarded to one side by the arbitrators, and were disallowed by the superior court because neither party had submitted argument thereon or otherwise contemplated that issue as part of the scope of their dispute.

From an equitable perspective, Petitioner has failed at all three appellate reviews of this intended "binding and final" arbitration award to explain why it failed to object to punitive damages, and/or raise New York law, in the underlying arbitration, thereby affording both parties the opportunity to brief the issue of the inclusion of punitive damages for the arbitrators up front. It is sheer speculation now to argue that the existing amount of the compensatory award[2], and/or the denial of attorneys' fees, would have remained so had the arbitrators known their award would be cut in half by a

[2] Note that the $27,000.00 compensatory damage award was far below the actual relief requested: See Award, C1, p. 16: RELIEF REQUESTED. Claimant Requested: Compensatory damages in the amount of $111,170.04, punitive damages and attorneys fees."

brokerage "lying in the grass" with questionable defenses asserted as sheer afterthought. Hence, it is neither legally permissible nor procedurally equitable to "rewrite" the arbitration award when Petitioner has otherwise failed to allege fraud by the parties or dishonesty by the arbitrator. United Paper Workers Intl. Union, AFL-CIO, et al. v. Misco, Inc., (1987) 484 U.S. 29, 98 L.Ed.2d 286, 298.

II. HASLIP DUE PROCESS CONSIDERATIONS ARE NOT INVOKED THROUGH A SECURITIES ARBITRATION

Appellant misconstrues the recent burst of attention on the viability of punitive damages in jury trials as an excuse to avoid its problematic waiver of the New York law issue, relying on the Haslip opinion in claiming its "due

process" right was violated through award of punitive damages and that such a constitutional right can never be waived. Yet the law is clear that all defenses in an arbitration must be affirmatively raised or be lost. Beckett v. Kaynar Mfg. Co., Inc. (1958) 49 Cal.2d 695, 699-700; O'Malley v. Petroleum Maintenance Co. (1957) 48 Cal.2d 107, 110; Hydrothermal Energy Corp. v. Fort Bidwell Indian Community Council (1985) 170 Cal.App.3d 489, 497. In the present matter the alleged violation of due process did not arise after the fact from the award itself, but rather was ascertainable from the outset by the very submission and consideration of punitive damages as a remedy. Hence, waiver in this matter cannot be pushed aside as a mere procedural defense dwarfed by the constitutional proportions of due process.

As stated by the court in Todd Shipyard Corp. v. Cunard Line, Ltd. (9th Cir. 1991) 943 F.2d 1056, which rejected the losing party's claim that an award of punitive damages violated its due process:

> Cunard had every opportunity to present evidence, to argue the merits of its position, and to challenge the arbitrator's award of court. Having taken advantage of this process, into which it entered voluntarily, Cunard cannot now argue that its due process was denied. (943 F.2d at 1064.)

Haslip has no application to alternative dispute resolution, which is bottomed on entirely different public policy considerations than were invoked through the Alabama statutes analyzed in Haslip. Note that California has already passed upon and upheld the constitutionality of its punitive damage

provisions post-Haslip in Las Palmas Assocs. v. Las Palmas Center Assocs. (1991) 235 Cal.App.3d 1220, 1256-1259.

The only case even remotely on point with the matter before this Honorable Court is Lee v. Chica, 983 F.2d 883, petition for rehearing and rehearing in banc denied, March 4, 1993, cert. denied, 114 S.Ct. 287 (1993). In Lee, the majority began by observing that judicial review of arbitration awards is narrowly limited and an arbitration award will not be set aside unless it is completely irrational or evidences a "manifest disregard for law." (Id. at 885.) Concerning punitive damages, the claimant argued on appeal that the district court erred in disallowing punitive damages because American Arbitration Association rules (which controlled in that securities arbitration) allowed arbitration panels to

award punitive damages and because federal courts have upheld arbitral awards of punitive damages. The appeals court majority sided with the claimant and concluded essentially that because some circuits have held (and the majority agreed) that "AAA arbitrators may grant any remedy or relief including punitive damages", and because AAA Rule 43 specifically allows arbitrators to award "any remedy or relief that the arbitrator deems just and equitable," the district court had erred in vacating the punitive damage award. (Id. at 887.)

Note that in Lee v. Chica, the respondent argued that the law of Minnesota, where the arbitration occurred, prohibited an award of punitive damages by an arbitration panel and that the arbitration clause in the customer agreement incorporated Minnesota law as

the law governing the contract. While the National Association of Securities Dealers ("NASD") Code of Arbitration Procedure, which governs the within arbitration, is not per se as broadly worded as AAA Rule 43, the submission to arbitration [C8, pp. 156-158] clearly makes no reference to excluding punitive damages or to application of New York law, and in fact provided at ¶1 thereof that the parties "hereby submit the present matter in controversy as set forth in the attached statement of claim, answer, cross-claims and all related counter-claims and/or third party claims as may be asserted, to arbitration in accordance with the Constitution, By Laws, Rules, Regulations and/or Code of Arbitration Procedure of the sponsoring organization." The NASD rules do not in any way limit the remedies available or the scope of the arbitrators'

powers and, in fact, refer to "novel theories" of remedies in connection with presentation of trial briefs. (C9:192-211 at 208.)

Further, in the present matter it is clear that California law does not in any way (unlike that of Minnesota) limit the availability of punitive damages. Indeed, Moncharsh confirms that "[a]rbitrators, unless specifically required to act in conformity with rules of law, may base their decision upon broad principles of justice and equity, and in doing so may expressly or impliedly reject a claim that a party might successfully have asserted in a judicial action. (Citations omitted.)" Id. at 10. Further, "the arbitrators are not bound to award on principles of dry law, but may decide on principles of equity and good conscience, and may make their awards ex aequo et bono

[according to what is just and good]. (Citations omitted.)" Id. at pp. 10-11. Importantly, California law specifically entitles arbitrators to award punitive damages as long as they are not expressly excluded. Tate v. Saratoga Savings & Loan Assn., (1989) 216 Cal.App.3d 843, 855; see also, Baker v. Sadick (1984) 162 Cal.App.3d 618, 626, 630.

While Petitioner claims that Lee v. Chica is distinguishable in that it failed to analyze the due process ramifications enunciated in Haslip, the Haslip opinion is in fact not applicable to alternative dispute resolution. Since the Haslip opinion concludes that punitive damages are not per se unconstitutional in the jury trial context, it seems probable that the Supreme Court would likewise conclude that punitive damages are not per se unconstitutional in the contractual

arbitration context, although the Supreme Court has never addressed the issue except, by analogy, in approving arbitration of treble damages in anti-trust and RICO[3] cases. See, Mitsubishi Motors Corp. v. Solar Chrysler-Plymouth, (1985) 473 U.S. 638, 105 S.Ct. 3346, 3358, 87 L.Ed.2d 444; Shearson Amer. Express v. McMahon, (1987) 482 U.S. 220, 107 S.Ct. 2332, 2344, 96 L.Ed.2d 185. Hence, the dissent in Lee v. Chica on which Petitioner relies finds no apparent support in Haslip for its argument that arbitrators should be flatly denied any authority to impose punitive damages on constitutional grounds. (Id. at 889.)

Nor similarly is there any language in Haslip directly addressing whether the

[3] RICO claims are based on the Racketeer Influenced Corrupt Organizations Act, 18 U.S.C. §§1961, et seq.

limited scope of discovery before arbitrations or loose application of rules of evidence in arbitrations has any relevance to the constitutionality of punitive damage awards in arbitration cases. Hence, the dissent in Lee v. Chica once again flounders in citing Haslip for its argument that punitive damages should not be allowed in arbitrations because of limited discovery and/or loose applications of rules of evidence in arbitrations.

As in Lee v. Chica, the matter before this court is strictly one of private contract and agreement between the parties, limited only by: (1) the submission to arbitrate (C8, pp. 166-168, which was not the Cash Account agreement); (2) the NASD rules under which the arbitration was held; and (3) the procedural law of the State of California,

none of which excludes punitive damages. Further, federal policy, invoked through application of the Federal Arbitration Act [9 U.S.C. §2], supports vesting arbitrators with the authority to award punitive damages if the parties' agreement contemplates such an award. Todd Shipyards Corp., supra, 943 F.2d at 1062-63; Bonar v. Dean Witter Reynolds, Inc. (11th Cir. 1988) 835 F.2d 1978, 1987; Raytheon Co. v. Automated Business Systems, Inc., (1st Cir. 1989) 882 F.2d 6, 11-12; Willoughby Roofing & Supply v. Kajima Intern. (N.D. Ala. 1984) 598 F.Supp. 353, 360, aff'd in (11th Cir. 1985) 776 F.2d 269.

III. APPELLANT IS ATTEMPTING TO FOIST NEW YORK LAW UPON CALIFORNIA AND OVERRULE WITHOUT AUTHORITY CALIFORNIA'S PRONOUNCEMENT ON CHOICE OF LAW PROVISIONS

The appellate opinion correctly noted at p. A13, fn. 6, that "[t]he parties concede that the New York prohibition on punitives was not argued in the arbitration proceedings." However, California has already mandated that, even in the presence of New York law, there would be no change in the outcome of this arbitration, as California will follow only the substantive law of New York and not its procedural restrictions on arbitrations. Bonar, supra, 835 F.2d at 1987; Willoughby Roofing & Supply, supra, 598 F.2d at 359; Raytheon Co., supra, 882 F.2d at 11, fn. 5; Willis v. Shearson/American Express, Inc. (M.D. N.C. 1983) 569 F.Supp. 821, 824; Singer v. E.F. Hutton & Co., Inc. (S.D. Fla. 1988) 699 F.Supp. 276, 279.[4] Appellant cites absolutely no authority requiring the rest of the United States to follow a single 20-year old opinion out of New York in the face of the issue's previous consideration and rejection as part of California's overall philosophy of alternative dispute resolution through arbitration.

The preprinted, unilaterally presented Cash Account agreement between the parties, the language over which the complaining Petitioner had complete and

[4] The California appellate court declined to follow two Second Circuit cases, Barbier v. Shearson Lehman Hutton, Inc. (2nd Cir. 1991) 948 F.2d 117, 122 and Fahnestock & Co. v. Waltman (2nd Cir. 1991) 935 F.2d 512, 518, which held, contrary to the cases cited above, that state law relating to the propriety of a punitive damages award by an arbitrator is not preempted by federal substantive law, and thus vacated the punitive damage awards.

total control, did not preclude punitive damages: If its innocuous reference to "New York law" was intended as a devious remedy limitation, it was apparently unaware that California had already rejected such sly tactics in adhering under these circumstances to New York substantive law only.

CONCLUSION

The arbitration award in this matter is final and binding and should not be the subject of a third appellate review. New York law did not apply herein and, even if it did, it was only the substantive and not procedure law thereof, which does not preclude punitive damages. Lastly, the Haslip decision is not controlling in this matter and does not invoke procedural due process considerations. The opinion of the California Court of Appeals for the

Second Appellate District should therefore be affirmed.

Respectfully submitted,

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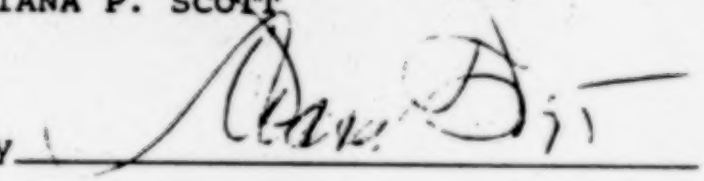
By 

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